AUDIT REFERRAL # 04-07

FEDERAL ELECTION COMMISSION
WASHINGTON, D C 20463

September 23, 2004

MEMORANDUM

TO: Lawrence H. Norton
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SUBJECT: Democratic Party of Hawaii (A03-28) – Referral Matters

On September 14, 2004, the Commission approved the final audit report on the Democratic Party of Hawaii. The final audit report includes the following matters

Finding 1 – Receipt of Prohibited Contributions
Finding 2 – Receipt of Contributions that Exceed Limits
Finding 4 – Allocable Expenses Paid from Non-federal Accounts

All workpapers and related documentation are available for review in the Audit Division. Should you have any questions regarding this matter, please contact Rhonda Gillingwater or Alex Boniewicz at 694-1200.

Attachments: Finding 1 – Receipt of Prohibited Contributions
Finding 2 – Receipt of Contributions that Exceed Limits
Finding 4 – Allocable Expenses Paid from Non-federal Accounts

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Part IV
Findings and Recommendations

Finding 1. Receipt of Prohibited Contributions

Summary
DPH received two contributions totaling $30,000 from the non-federal accounts of two political action committees. The Audit staff recommended DPH provide evidence that these contributions are not from prohibited sources or transfer the funds from the federal account to the non-federal account. In response to the interim audit report, DPH did not dispute that the two contributions were impermissible and had been inadvertently deposited into the federal account. In addition, DPH filed amended disclosure reports which included Schedules D that list these items as debt payable to the non-federal account.

Legal Standard
A. Federal v. Non-Federal Account. The federal account may contain only those funds that are permissible under the federal election law; the non-federal account may contain funds that are not permitted under the federal law (but are legal under state law), such as contributions that exceed the limits of the federal law and contributions from prohibited sources, such as corporations and labor organizations. 11 CFR §102.5(a)(1)(i) and (a)(3).

B. Questionable Contributions. If a committee receives a contribution that appears to be prohibited (a questionable contribution), it must follow the procedures below:

1. Within 10 days after the treasurer receives the questionable contribution, the committee must either:
   - Return the contribution to the contributor without depositing it; or
   - Deposit the contribution (and follow the steps below). 11 CFR §103.3(b)(1).
2. If the committee deposits the questionable contribution, it may not spend the funds and must be prepared to refund them. It must therefore maintain sufficient funds to make the refunds or establish a separate account in a campaign depository for possibly illegal contributions. 11 CFR §103.3(b)(4).
3. The committee must keep a written record explaining why the contribution may be prohibited and must include this information when reporting the receipt of the contribution. 11 CFR §103.3(b)(5).
4. Within 30 days of the treasurer's receipt of the questionable contribution, the committee must make at least one written or oral request for evidence that the contribution is legal. Evidence of legality includes, for example, a written statement from the contributor explaining why the contribution is legal or an oral explanation that is recorded by the committee in a memorandum. 11 CFR §103.3(b)(1).
5. Within these 30 days, the committee must either:
   - Confirm the legality of the contribution; or
   - Refund the contribution to the contributor and note the refund on the report covering the period in which the refund was made. 11 CFR §103.3(b)(1).

Facts and Analysis

A review of all contributions from party and other political committees resulted in the identification of two impermissible contributions totaling $30,000. DPH received $25,000 from a non-federal account of a union political committee on October 28, 2002, designated for its non-federal account; and, $5,000 from a non-federal account of a political action committee on November 19, 2002. It is the opinion of the Audit staff that the contributions were deposited into the federal account in error.

Based on the Audit staff's analysis of DPH bank account balances, those balances were insufficient to refund the prohibited contributions between December 2, 2002, and the end of the audit period. The balance in DPH's bank accounts on December 31, 2002, was $13,507,[1] insufficient to refund both of the prohibited contributions and the excessive contributions addressed at Finding 2 below.

The Audit staff advised DPH's treasurer of the prohibited contributions. The treasurer was unaware of the impermissible nature of the contributions, but indicated a willingness to make the necessary refunds.

Interim Audit Report Recommendation and Committee Response

The Audit staff recommended that DPH provide evidence that the two contributions ($30,000) are not prohibited. Absent such evidence, DPH should have transferred $30,000 from the federal account to the non-federal account, as it was intended, and provided evidence of the transfer (photocopies of the front and back of the negotiated instrument). If funds were not available to make the necessary refunds, the amounts due should have been disclosed on Schedule D (Debts and Obligations Excluding Loans) until funds became available to make the refunds. In response to the interim audit report, DPH did not dispute that these contributions were impermissible and acknowledged that they were inadvertently deposited into the federal account. DPH also filed amended disclosure reports which included Schedules D, listing these items as debts owed to the non-federal account.

Finding 2. Receipt of Contributions that Exceed Limits

Summary

DPH received nine contributions that exceeded limitations by $51,000. Four refunds ($20,000) were made, but not timely. The Audit staff recommended that DPH provide evidence that the remaining contributions were not in excess of the limitations or refund the remaining $31,000. In response to the interim audit report, DPH did not dispute the majority of the contributions were excessive nor that the four refunds were made untimely. DPH did provide information which proved that one contribution from a political action committee in the amount of $5,000 was not excessive. DPH also filed amended disclosure reports that included Schedules D which listed the remaining excessive contributions ($26,000) as debt.

[1] DPH reported its ending cash on hand on August 29, 2004, to be $69,639.

Legal Standard

A. Party Committee Limits. A party committee may not receive more than a total of $5,000 per year from any one contributor. 2 U.S.C. §§441a(a)(1)(C), (2)(C) and (f); 11 CFR §§110.1(a) and (d) and 110.9(a).

B. Handling Contributions That Appear Excessive. If a committee receives a contribution that appears to be excessive, the committee must either:

- Return the questionable check to the donor; or
- Deposit the check into its federal account and:
  - Keep enough money in the account to cover all potential refunds;
  - Keep a written record explaining why the contribution may be illegal;
  - Include this explanation on Schedule A if the contribution has to be itemized before its legality is established;
  - Seek a reattribution or a redesignation of the excessive portion, following the instructions provided in Commission regulations; and
  - If the committee does not receive a proper reattribution or redesignation within 60 days after receiving the excessive contribution, refund the excessive portion to the donor. 11 CFR §§103.3(b)(3), (4) and (5) and 110.1(k)(3)(ii)(B).

C. Revised Regulations Applied. The Commission recently adopted new regulations that allow committees greater latitude to reattribute contributions to joint account holders and has decided to apply these regulations to current matters. The Audit staff has evaluated the excessive contributions discussed below using the new regulations.

Facts and Analysis

The Audit staff's review of contributions identified $51,000 of contributions in excess of allowable limits had been accepted; five from individuals ($31,000) and four from political committees ($20,000). DPH has refunded $20,000 to four contributors; however, these refunds were untimely, with one of the refunds being made 16 months after the contribution was deposited.

As noted in Finding 1 above, beginning in December 2002, DPH did not maintain sufficient funds to make all refunds. The balance in DPH's bank accounts on December 31, 2002 was $13,507.[2]

The Audit staff provided DPH's treasurer with a schedule of the excessive contributions noted above. A discussion ensued about refunding the remaining excessive contributions and how to disclose them as a debt until sufficient funds were available to make the refunds.

Interim Audit Report Recommendation and Committee Response

The Audit staff recommended that, DPH:

- Provide evidence that the identified contributions were not excessive; or

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[2] See Footnote 2.

- Refund the remaining $31,000 and provide evidence of such refunds (copies of the front and back of each negotiated refund check).
- If funds were not available to make the necessary refunds, amended reports were to be filed to reflect the amounts to be refunded as debts on Schedule D (Debts and Obligations Excluding Loans) until funds became available to make the refunds.

In response to the interim audit report, DPH did not dispute the majority of the excessive contributions nor the fact that the four refunds previously made were untimely. DPH did provide information which proved that one contribution from a political action committee in the amount of $5,000 was not excessive. DPH also filed amended disclosure reports that included Schedules D which listed the remaining $26,000 as debt. \

Finding 4. Allocable Expenses Paid from Non-federal Accounts

Summary

DPH made 54 disbursements ($164,640) from its two non-federal accounts that appear to be for allocable expenses. The Audit staff recommended that DPH demonstrate that these disbursements were not allocable expenditures or amend its disclosure reports to include these disbursements. In response to the interim audit report, DPH filed amended reports disclosing these items.

Legal Standard

A. Paying for Allocable Expenses. Commission regulations offer party committees two ways to pay for allocable, shared federal/non-federal expenses.

- They may pay the entire amount of the shared expense from the federal account and transfer funds from the non-federal account to the federal account to cover the non-federal share of that expense; or

- They may establish a separate, federal allocation account into which the committee deposits funds from both its federal and non-federal accounts solely for the purpose of paying the allocable expenses of shared federal/non-federal activities. 11 CFR §106.5(g)(1)(i) and (ii)(A).

B. Reporting Allocable Expenses. A political committee that allocates federal/non-federal expenses must report each disbursement it makes from its federal account (or separate allocation account) to pay for a shared federal/non-federal expense. Committees report these kinds of disbursements on Schedule H-4 (Shared federal/Non-federal Activities). 11 CFR §104.10(b)(4).

C. Allocation Ratio for Administrative & Generic Voter Drive Costs. State and local party committees must allocate their administrative expenses and generic voter drive costs according to the ballot composition method. Under this method, a committee determines the ratio of federal offices to the total number of federal and non-federal offices expected on the ballot in the next general election in the state or geographic area. 11 CFR §106.5(d)(1) and (2).

Facts and Analysis

The Audit staff identified 54 payments ($164,640) made from DPH's two non-federal accounts, for such purposes as television and radio production, television advertising, research, postage and consulting. Documentation, such as invoices, bills and receipts, was either not available or did not demonstrate that these expenditures were for solely non-federal activities

The Audit staff's analysis indicated that during the audit period the non-federal account transferred significantly less than it could have to the federal account for its share of allocable expenses. A total of $275,636 was transferred; however, the non-federal share of allocated costs was $603,431, leaving an additional $327,795 which could have been transferred. Therefore, no transfer of funds by DPH to its non-federal account is required for $164,640 in allocable expenses paid for by the non-federal account.

At the exit conference, DPH's treasurer was provided a schedule of these disbursements and advised that absent documentation to demonstrate that they are not allocable expenses, the disbursements would need to be disclosed on Schedules H-4. The treasurer stated that these were not for shared expenses. She stated that for the 2002 election cycle, most of the party activity had been directed at state and local races, specifically the race for the governor's seat. She stated that she would provide the requested documentation.

Interim Audit Report Recommendation and Committee Response

The Audit staff recommended that DPH provide documentation supporting the solely non-federal nature of the above noted expenditures. Absent such a demonstration, the Audit staff recommended that DPH amend its reports to disclose these expenditures as memo entries on Schedules H-4. In response, DPH filed amended its disclosure reports as recommended.